

SECTION V:

**CONSOLIDATED FINANCIAL STATEMENTS,
NOTES AND SUPPLEMENTAL SCHEDULES**

U.S. Department of Health and Human Services
Consolidated Statement of Financial Position
As of September 30, 1997

	<i>(in millions)</i>					
	Education, Training and Social Services	Health	Medicare	Income Security	Admin. of Justice	Totals
Assets						
Entity Assets:						
Fund Balances with Treasury (Note 2)	\$ 9,275	\$ 33,086	\$ 183	\$ 13,767	\$ 34	\$ 56,345
Investments (Note 3)	-	1,206	151,085	-	-	152,291
Accounts and Loans Receivable, Net: (Note 4)						
From Federal Agencies	3	1,291	148	33	1	1,476
From the Public	1	447	2,448	19	1	2,916
Interest Receivable	-	-	2,849	-	-	2,849
Advances: (Note 5)						
To Federal Agencies	17	106	-	13	-	136
To the Public	6	87	10	-	-	103
Inventories	-	74	-	-	-	74
Property, Plant and Equipment, Net (Note 6)	-	1,302	38	-	-	1,340
Non-Entity Assets:						
Accounts Receivable, Net (Note 4)	-	136	-	-	-	136
Total Assets	<u>\$ 9,302</u>	<u>\$ 37,735</u>	<u>\$ 156,761</u>	<u>\$ 13,832</u>	<u>\$ 36</u>	<u>\$ 217,666</u>
Liabilities						
Funded Liabilities:						
Payables: (Note 7)						
Due Federal Agencies	\$ 1	\$ 219	\$ 126	\$ 8	\$ -	\$ 354
Due the Public	13	16,549	27,612	21	1	44,196
Advances: (Note 5)						
From Federal Agencies	275	182	-	-	1	458
From the Public	242	450	-	63	-	755
Accrued Payroll and Benefits	6	104	14	5	1	130
Unfunded Liabilities:						
Annual Leave	12	233	21	15	1	282
Workers' Compensation Benefits (Note 8)	3	143	7	11	3	167
Other Liabilities	-	24	-	-	-	24
PHS Commissioned Corps Pension (Note 9)	-	3,296	-	-	-	3,296
Total Liabilities	<u>552</u>	<u>21,200</u>	<u>27,780</u>	<u>123</u>	<u>7</u>	<u>49,662</u>
Net Position (Note 10)						
Unexpended Appropriations	8,468	17,528	-	13,696	37	39,729
Invested Capital	-	1,706	38	-	-	1,744
Cumulative Results of Operations	297	997	128,971	39	(4)	130,300
Future Funding Requirements	(15)	(3,696)	(28)	(26)	(4)	(3,769)
Total Net Position	<u>8,750</u>	<u>16,535</u>	<u>128,981</u>	<u>13,709</u>	<u>29</u>	<u>168,004</u>
Total Liabilities & Net Position	<u>\$ 9,302</u>	<u>\$ 37,735</u>	<u>\$ 156,761</u>	<u>\$ 13,832</u>	<u>\$ 36</u>	<u>\$ 217,666</u>

The accompanying notes are an integral part of these statements.

U.S. Department of Health and Human Services
Consolidated Statement of Operations and Changes in Net Position
For the Fiscal Year Ended September 30, 1997

	(in millions)					
	Education , Training and Social Services	Health	Medicare	Income Security	Admin. of Justice	Intra- HHS
						Totals
Revenues and Financial Sources						
Appropriated Capital Used:						
General Appropriations	\$ 12,786	\$ 120,814	\$ -	\$ 19,843	\$ 56	\$ -
Federal Matching Contributions (Note 11)	-	-	59,615	-	-	-
Employment Taxes	-	-	112,742	-	-	-
SMI Premiums Collected (Note 11)	-	-	19,141	-	-	-
Interest Revenue	-	-	11,900	-	-	-
Sales of Goods and Services	11	1,620	-	88	15	(334)
Imputed Financing	14	327	10	1	-	(40)
Other Revenue and Financing	-	293	5,947	-	-	-
Total Revenue and Financing Sources	12,811	123,054	209,355	19,932	71	(374)
Expenses						
Operating:						
Personnel Costs	129	3,316	1,217	117	16	(313)
Travel and Transportation	3	134	5	9	-	-
Rent, Communications and Utilities	17	333	41	17	2	-
Printing and Reproduction	-	29	18	-	-	-
Contractual Services	108	4,090	1,437	430	1	(10)
Supplies and Materials	3	686	6	5	-	(11)
Grants	12,526	113,634	35	19,356	40	-
Insurance Claims and Indemnities (Note 12)	-	137	207,455	-	-	-
Other Operating Expenses	-	41	-	-	-	-
Depreciation and Amortization	-	80	10	-	-	-
Imputed Personnel Costs	14	327	10	1	-	(40)
Other Non-Operating Expenses	2	142	1,677	-	-	-
Total Expenses	12,802	122,949	211,911	19,935	59	(374)
Excess of Revenues and Financing Sources	9	105	(2,556)	(3)	12	(2,433)
Net Position, Beginning Balance	10,831	22,205	121,899	10,588	22	165,545
Adjustments (Note 13)	(2,750)	3,361	9,638	(4,537)	(1)	5,711
Net Position, Restated Beginning Balance	8,081	25,566	131,537	6,051	21	171,256
Excess of Revenues and Financing Sources	9	105	(2,556)	(3)	12	(2,433)
Non-Operating Changes	660	(9,136)	-	7,661	(4)	(819)
Net Position, Ending Balance	\$ 8,750	\$ 16,535	\$ 128,981	\$ 13,709	\$ 29	\$ 168,004

The accompanying notes are an integral part of these statements.

U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES
NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS
AS OF SEPTEMBER 30 1997

1. SIGNIFICANT ACCOUNTING POLICIES

Basis of Presentation

The financial statements have been prepared to report the financial position and results of operations of HHS as required by the Chief Financial Officers Act of 1990 as amended by the Government Management Reform Act of 1994. They have been prepared from Departmental records in accordance with the form and content guidance of OMB, and follow the hierarchy of accounting principles and standards as specified. These statements are therefore different from financial reports prepared pursuant to other OMB directives that are primarily used to monitor and control HHS's use of budgetary resources.

Statements of cash flows and statements of budgetary resources and actual expenses are not included as principal financial statements for HHS and OPDIV reports. The OMB approved HHS's request to waive these requirements for FY 1997 reporting.

The financial statements consolidate the balances of about one hundred forty discrete appropriations and fund accounts, plus a number of accounts used for suspense, collection of receipts and general Governmental functions. Material intra-HHS balances have been eliminated in the consolidation of the account balances from the financial statements of HHS's twelve OPDIVs; each issued under separate cover. Summary elimination transactions are presented on the statement of operations and changes in net position; such transactions for the statement of financial position were considered to be immaterial in total and were not presented. Supplemental information is accumulated from the OPDIV reports, regulatory reports and other sources within HHS. Information is generally presented herein on a summary level, hence, greater detail on OPDIV programs and activities is found in the annual reports prepared by the OPDIVs.

Basis of Accounting

For most HHS programs, transactions are generally recorded on an accrual accounting basis and a budgetary basis. The cash basis is used by HCFA for Medicare benefit payments and for Medicaid Program draws by States to cover current quarter expenses. For both programs, an accrual method adjustment is made by recording year-end estimates of unpaid liabilities. Under the accrual method, revenues are recognized when earned and expenses are recognized when a liability is incurred, without regard to the receipt or payment of cash. Budgetary accounting facilitates compliance with legal constraints and controls over the use of federal funds.

Reporting Entity

The Department of Health and Human Services is comprised of twelve (12) OPDIVs all having diverse missions and programs

Health Care Financing Administration (HCFA)
Administration for Children and Families (ACF)
National Institutes of Health (NIH)
Health Resources and Services Administration (HRSA)
Centers for Disease Control (CDC)/Agency for Toxic Substances and Disease Registry (ATSDR)
Substance Abuse and Mental Health Administration (SAMHSA)
Indian Health Administration (IHS)
Food and Drug Administration (FDA)
Administration on Aging (AoA)
Agency for Health Care Policy and Research (AHCPR)
Program Support Center (PSC)
Office of the Secretary (OS)

In FY 1997 the first eight OPDIVs listed above received full scope audits, while the last four were reviewed as part of the Departmental consolidated audit.

Terminology

Certain terms are used on the statement of financial position which may be unfamiliar to readers who are not working within the Federal financial community: Entity assets are those assets which the reporting entity holds and has the authority to use in its operations; ***Non-entity*** assets are those the entity holds but does not have the authority to use; ***Unfunded*** liabilities are those for which budget authority has not been received; ***Future Funding Requirements*** is a component of net position disclosing the sum of all unfunded liabilities of the entity.

Fund Balances with Treasury

HHS does not maintain cash in commercial bank accounts. The U.S. Treasury processes cash receipts and disbursements for HHS. The balance of this account primarily represents amounts available to pay agency liabilities.

Investments

Trust fund balances in excess of current needs are invested in interest-bearing obligations of the United States or in obligations guaranteed as to both principal and interest by the United States.

Accounts and Loans Receivable

Accounts receivable consist of amounts owed to the Department by other Federal agencies and the public. Amounts due from the public are presented net of allowances for uncollectable accounts. The estimate of an allowance is based on past collection experience and/or an analysis of the outstanding balances.

Loans are accounted for as receivables after funds are disbursed. In accordance with Credit Reform legislation, for loans obligated prior to October 1, 1991, loan principal, interest, and other costs are reduced by an allowance for estimated uncollectable amounts based on historical data and current market factors.

For loans obligated on or after October 1, 1991, the loans receivable is reduced by an allowance equal to the present value of the subsidy costs associated with these loans.

Inventories

HHS maintains inventories almost entirely for consumption by the purchasing OPDIV or other HHS components. Most inventories are of a medical nature, consisting of such materials as pharmaceuticals, medical supplies, biological products and vaccines. Generally, these inventories are recorded at (1) the lower of cost (using weighted-average cost method) or market, or (2) historical cost.

Property Plant and Equipment

Property and equipment purchases and additions are valued at cost. Equipment is capitalized when its cost is \$25,000 or more and it has a useful life of more than two years. The change in the capitalization threshold from \$5,000 to \$25,000 was effective in Fiscal Year 1997 in accordance with Statements of Federal Financial Accounting Standards (SFFAS) No. 6, "Accounting for Property, Plant and Equipment." Both property and equipment are depreciated on a straight-line basis over the estimated useful life of the item. Land is not depreciated. Normal maintenance and repair costs are expensed as incurred.

Liabilities

Liabilities are recognized for amounts of probable future outflows or other sacrifices of resources as a result of past transactions or events. Since HHS is a component of the U.S. Government, a sovereign entity, its liabilities cannot be liquidated without legislation that provides resources to do so.

Payments of all liabilities other than contracts can be abrogated by the sovereign entity.

Unfunded liabilities are incurred when funding has not yet been made available through Congressional appropriations or current earnings. HHS recognizes such liabilities for employee annual leave earned but not taken, amounts billed by the Department of Labor for Federal Employee's Compensation Act (disability) payments, and for Medicaid audit disallowances under appeal and for deferrals. The total unfunded liability equals the future funding requirements provision in the net position. For HHS revolving funds, all liabilities are funded as they occur.

In accordance with Public Law and existing Federal accounting standards, no liability is recorded for any future payment to be made on behalf of current workers contributing to the Medicare Hospital Insurance (HI) Trust Fund.

Retirement Plans

Most HHS employees participate in the Civil Service Retirement System (CSRS) or the Federal Employee Retirement System (FERS). Under CSRS, HHS makes matching contributions equal to 7 percent of basic pay. For FERS employees, HHS contributes the employer's matching share for Social Security and contributes an amount equal to one percent of employee pay to a savings plan and matches up to an additional 4 percent of pay. Most employees hired after December 31, 1983 are covered by FERS. The Office of Personnel Management reports on CSRS and FERS assets, accumulated plan benefits, unfunded liabilities, if any, applicable to Federal employees.

The HHS-administered PHS Commissioned Corps Retirement System is discussed in Note 8, "Pension Liability".

Leave

Annual leave is accrued as it is earned, and the accrual is reduced as leave is taken. The accrual for accumulated annual leave is based on current year pay rates. Sick leave and other types of leave are expensed as leave is taken.

Obligations Related to Canceled Appropriations

Payments may be required of up to 1% of current year appropriations for valid obligations incurred against appropriations that have been canceled. The total potential payments related to canceled appropriations is estimated to be \$409.2 million as of September 30, 1997.

Revenues and Financing Sources

Congressional appropriations are the primary funding source for most of the Department's programs. For financial statement purposes, appropriations are recognized as a financing source as expenses are incurred.

Medicare's HI Trust fund is financed by a 1.45 percent tax required to be paid by U.S. employers and by employees. The Supplemental Medical Insurance (SMI) Trust fund receives premium payments from Medicare beneficiaries and these amounts are matched approximately 3 to 1 by Congressional appropriations. Interest revenue on investments is recognized as it is earned.

Reimbursable service agreements between HHS activities and with other Federal agencies generally recognize revenues when the related expenses are incurred. Revolving funds and reimbursable agreements recognize revenue when goods are delivered or services rendered. Various user fees are collected to offset the cost of providing services.

Imputed financing is the financing source for imputed personnel costs. This cost is an estimate of the pension and retirement benefits that current employees will (eventually) receive which exceed contributions made to retirement plans during the fiscal year. The estimate for Public Health Service (PHS) Commissioned Corps employees is an intra-HHS elimination because the PSC recognizes the liability for their retirement plan.

Use of Estimates in Preparing Financial Statements

The preparation of financial statements in accordance with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Intra-Governmental Relationships and Transactions

In the course of its operations, HHS has relationships and financial transactions with numerous Federal agencies. The more prominent of these are with the Social Security Administration (SSA) and the Department of the Treasury. The SSA determines eligibility for Medicare programs, and also allocates a portion of Social Security benefit payments to the Medicare Part B Trust Fund for Social Security beneficiaries who elect to enroll in the Medicare Part B program. The Treasury receives the cumulative excess of Medicare receipts and other financing over outlays, and issues interest-bearing securities in exchange for the use of those monies. At the Government-wide level, the assets related to the trust funds on HHS' financial statements and the corresponding liabilities on the Treasury's financial statements should be eliminated.

Comparative Data

Several factors have reduced the value of presenting comparative financial statements for FY 1997 and have led to management's decision not to present comparative data. These factors are that in FY 1997: 1) two OPDIVs were audited for the first time, 2) new accounting standards were implemented, and 3) intra-HHS transactions were eliminated for the first time.

2. FUND BALANCES WITH TREASURY

HHS's undisbursed account balances are listed below by fund type. Other funds include balances in deposit, suspense, clearing and related non-spending accounts.

	(In millions)	1997
Fund Type:		
Trust Funds	\$	295
Revolving Funds		651
Appropriated Funds		54,906
Other Funds		<u>493</u>
Totals		<u>\$ 56,345</u>

3. INVESTMENTS

HHS invests trust fund cash that is in excess of current needs in Department of the Treasury securities. The Treasury is HHS's agent and advisor for investing.

HCFA invests in Special Issues exclusive to HI and SMI Trust Funds that are purchased and redeemed at face value. Certificates are short-term and pay from 6 5/8 to 6 3/4 percent. Bond interest rates range from 6 1/4 to 13 3/4 percent. Bonds mature at various dates from June 1998 to June 2012. The accrued interest receivable on the investments totaled \$2,849 million as of September 30, 1997.

HRSA's Vaccine Injury Compensation Trust Fund invests in market-based (MK) special securities. Securities currently held are MK Bills maturing on August 20, 1998.

The NIH invests a portion of their trust fund cash in short-term U. S. Treasury Securities. The balances include principal and accrued interest.

	(In millions)	1997
Issue Type:		
HI Certificates	\$	1,838
SMI Certificates		114,783
HI Bonds		2,517
SMI Bonds		<u>31,947</u>
HCFA Totals		151,085
HRSA Bills		1,196
NIH Bills		<u>10</u>
Totals		<u>\$ 152,291</u>

The majority of HHS' investments in securities are held to maturity and no provision is made for unrealized gains and losses.

4. ACCOUNTS AND LOANS RECEIVABLE, NET

HCFA's Medicare receivables are primarily due to overpayments to providers, beneficiaries, physicians and suppliers, and to claims where Medicare should be secondary payer. The Medicaid balance is the net realizable value of disallowances in dispute with the States.

Loans receivable are included for the Health Education Assistance Loans (HEAL) guaranteed loan program which is administered by HRSA. The amount of gross receivables for this program represents defaulted loans, which have been paid to lenders under the guarantee, and includes principal and interest.

HHS non-entity receivable balances represent amounts that cannot be used by HHS once collected. Such receipts are transferred to the General Fund of the Department of the Treasury.

	(In millions)		1997
Program/Type	Gross Receivables	Allowances	Net Receivables
ENTITY:			
From Federal Agencies	<u>\$ 1,476</u>	<u>\$ -</u>	<u>\$ 1,476</u>
From the Public			
Medicare	\$ 5,517	\$ 3,069	\$ 2,448
Medicaid	32	-	32
HEAL Loans	498	132	366
Other Public	<u>81</u>	<u>11</u>	<u>70</u>
Total	<u>\$ 6,128</u>	<u>\$ 3,212</u>	<u>\$ 2,916</u>
NON-ENTITY:	<u>\$ 586</u>	<u>\$ 450</u>	<u>\$ 136</u>

5. ADVANCES

Assets

Most of HHS's advances to the public of \$103 million consist of advances for grant programs. A small portion of this amount is for employee travel and emergency salary advances. The advances to Federal agencies of \$136 million are for goods and services to be provided to HHS.

Advances to grantees are recorded either upon information provided by the grantees at the time the advance is drawn or by allocation, for pooled grants.

Advances for grant programs are liquidated upon the grantee's reporting of expenditures on the quarterly SF-272 report, which in many cases are received several months after the grantee actually incurs the expense reported thereon. In 1997, all OPDIVs, except HCFA, adopted a Department-wide accrual methodology to refine the method used to estimate and accrue amounts due grantees for expenses incurred but not reported. Accrual amounts were determined by PSC's Division of Payment Management (DPM), the manager of HHS's central grants payment system. When these accruals are greater than the amounts advanced to the grantee, the net amount is recorded as an accounts payable due the grantee (Payable Due the Public) and in some OPDIV records as an advance from the grantee (Advances from the Public).

Allocating Grantee Advances

In 1997, HHS implemented a new process for allocating pooled advances to OPDIV appropriations. The new process resulted in a one-time adjustment that redistributed the cash outlays recorded in Treasury records in order to agree with cash outlays computed through the new allocation process and recorded in the Payment Management System records. Appropriate entries were made to OPDIV accounting records.

Liabilities

Advances from other Federal agencies of \$458 million are for the provision of goods and services. Advances from the public of \$755 million are largely related to the excess of grant accruals over the amount advanced to grantees.

6. PROPERTY PLANT AND EQUIPMENT, NET

Balances for the major categories of HHS property and equipment are listed below, recognized at acquisition cost.

		(In millions)	1997
Category:	Cost	Accumulated Depreciation	Net Book Value
Land	\$ 28	\$ -	\$ 28
Buildings	1,761	771	990
Equipment	<u>614</u>	<u>292</u>	<u>322</u>
Totals	<u>\$ 2,403</u>	<u>\$ 1,063</u>	<u>\$ 1,340</u>

7. PAYABLES

Payables of \$44,500 million comprise \$354 million due Federal agencies and \$44,196 million due the public as shown on the financial statement. In addition, we have classified payables of \$41,760 million as those associated with benefits and the remainder, \$2,790 million as other payables.

Benefits payable recognizes accrued entitlement benefits earned in the current (or prior) periods, but not yet paid. Other Payables are amounts owed for goods and services received, progress in contract performance, and rents due to others.

The balances below are all funded, i.e., budget authority has been received. Unfunded Medicaid benefits payable of \$5,609 million are presented under Other Liabilities.

	(In millions) 1997
Benefits Payable:	
Medicare Claims	\$ 27,612
Medicaid	14,148
Other:	
Grant Advances Payable	1,201
Accounts Payable	1,000
Loan Guarantees	353
Vaccine Liability Claims	<u>236</u>
Total Payables	<u>\$ 44,550</u>

8. WORKERS' COMPENSATION BENEFITS

The liability for future workers' compensation (FWC) benefits includes the expected liability for death, disability, medical and miscellaneous costs for approval compensation cases. The amount of this liability is provided to HHS by the administrators of Workers' Compensation Benefits (Federal Employees Compensation Act), the Department of Labor. The liability was determined using a method utilizing historical benefit payment patterns related to a specific incurred period to predict the ultimate payment related to that period. Consistent with past practice, these projected annual benefit payments have been discounted to present value using the Office of Management and Budget's June 10, 1997 economic assumptions for 10-year Treasury notes and bonds. Interest rate assumptions utilized for discounting were as follows:

1997

6.24% in year 1
 5.82% in year 2
 5.60% in year 3
 5.45% in year 4
 5.40% in year 5
 and thereafter

In FY 1997 the FWC actuarial model was revised to include additional features that would provide a more accurate estimation of the FECA FWC liability. A wage inflation factor and medical inflation factor were added and applied to the calculation for projected future payments. Historical factors were used to adjust the model's historical payment streams to current year constant dollars. From this constant year data, retention rates were developed and applied to current year accrual payments as were future inflation factors for wages and medical costs. Also incorporated into the model was a discounting formula to recognize the timing of accrual compensation payments. In Fiscal Year 1997, the period of time covered by the calculation was increased from 23 to 37 years.

9. PHS COMMISSIONED CORPS PENSION

HHS administers the PHS Commissioned Corps Retirement System for approximately 6,100 active duty officers and 3,600 retiree annuitants or survivors. Authorized by Public Law 78-410, it is a defined benefit plan and is non-contributory. The plan does not have accumulated assets, funding is provided entirely on a “pay as you go” basis by Congressional appropriations. Administrative costs are not borne by the plan. The actuarial present value of accumulated plan benefits is \$3,296 million, of which \$499 million is non-vested. The assumed interest rate is 6.75 percent. Economic assumptions are the same as those used by the Military Retirement System. Withdrawal and retirement rates are based on the historical trends of officers in the PHS retirement system.

The actuarial liability was established based upon the Public Health Service’s Report for Commissioned Corps Retirement System for Plan Year Ending September 30, 1996.

10. NET POSITION

Net position is the difference between assets and liabilities. Unobligated appropriations are either available for obligation or not available (permanently or temporarily) pursuant to a specific provision in law. Undelivered orders represents appropriations obligated (i.e. legally reserved) for the amount of goods or services ordered but not yet received.

Invested capital represents the net investment of the Government in the Department. This includes the corpus of revolving funds, net book value of capital assets purchased with appropriations and donations. The cumulative results of operations represents the net difference between (1) expenses and losses and (2) financing sources, including appropriated capital used, and revenues and gains since the inception of the activity. The amount of funds required to liquidate the unfunded liabilities is shown as future funding requirements.

	(In millions)			1997
	Trust Funds	Revolving Funds	Appropriated Funds	Totals
Unexpended Appropriations: Unobligated, Available	\$ 31	\$ 296	\$ 8,375	\$ 8,702
Unavailable	-	-	29	29
Undelivered Orders	62	50	30,886	30,998
Invested Capital	39	410	1,295	1,744
Cumulative Results of Operations	130,077	(39)	262	130,300
Future Funding Requirements	____(30)	____(27)	____(3,712)	____(3,769)
Totals	<u>\$130,179</u>	<u>\$ 690</u>	<u>\$ 37,135</u>	<u>\$168,004</u>

11. SMI PREMIUMS COLLECTED

SMI benefits and administrative expenses are financed by monthly premiums paid by Medicare beneficiaries and matched by Federal appropriations. Section 1844 of the Social Security Act authorizes appropriated funds to match SMI premiums collected, and outlines the ratio for the match as well as the method to make the trust funds whole, if insufficient funds are available in the appropriation to match all premiums received in the fiscal year.

The monthly SMI premium for the first three months of fiscal year 1997 was \$42.50; the monthly premium for the remainder of the year was \$43.80. SMI Premiums collected from beneficiaries totaled \$19.1 billion in fiscal year 1997 (\$18.9 billion in fiscal year 1996) and were matched by a \$59.6 billion contribution from the Federal Government (\$54.7 billion in fiscal year 1996, restated).

12. INSURANCE CLAIMS AND INDEMNITIES

Of the \$207,455 recorded as Medicare claims expense, a portion is estimated to be improper payments. Federal Government audits require the review of programs for compliance with Federal laws and regulations. Accordingly, the OIG reviewed a statistically valid sample of Medicare claims to determine whether claims were paid properly by Medicare contractors, and whether services were actually performed and were medically necessary. The internal claims process involves reviewing claims as billed and paying the correct amount for the services rendered. A review of this process revealed an error rate of less than 2 percent. However, the external billing process had a dollar error rate in between \$12.1-28.4 billion (\$17.8-28.6 billion in fiscal year 1996). The majority of the errors fell into four broad categories: insufficient or no documentation, lack of medical necessity, non-covered or unallowable service, and incorrect coding. The audit was not performed in fiscal year 1995; therefore, the estimated improper payments are not presented for fiscal year 1995.

13. ADJUSTMENTS

HHS's net position had a net increase of \$5,711 million during fiscal year 1997 due to adjustments made which related to prior years' activities. The causes for these significant adjustments are varied in nature.

HCFA recorded an adjustment of \$9,638 million due to changing its method of estimating a liability for unpaid HI and SMI (Medicare) benefit claims as of September 30. HCFA's Office of the Actuary developed a new methodology to address concerns expressed by the Office of Inspector General in prior fiscal year audits. HCFA believes the methodology is reasonable and more appropriate for financial reporting.

An adjustment of \$5,609 million to increase the beginning balance of net position was required to record a prior year Medicaid funding source. This funding source was not recorded in FY 1996 because there was not a common agreement on whether the Medicaid expenses incurred but not reported as of September 30, 1996 were considered to be funded or unfunded. A review of the appropriation language by the Office of General Counsel, HCFA, resulted in the determination to record these as funded expenses. The total effect of the two adjustments is an increase in HCFA's net position of \$15,247 million.

During fiscal year 1997, in connection with the reconciliation of ACF's general ledger and balances maintained by the Division of Payment Management at September 30, 1997, it was determined that the grant advance asset amount reported in the financial statements at September 30, 1996 was overstated. The correction resulted in a reduction of ACF's net position of \$7,288 million.

Based on the recommendation of prior audits, HHS implemented a new accrual methodology for grants, as discussed in Note 5, "Advances". This change had a varying impact on the accounts of the grant-issuing OPDIVs. The NIH reduced net position by \$3,061 million; CDC had a grant accrual reduction of \$379 million and increases of \$67 million not associated with the accrual, to bring its adjustments to a net of \$312 million. Much smaller adjustments were necessary for the other OPDIVs.

Prior to fiscal year 1997, HRSA had not included the post-1988 claim liabilities or related assets of the Vaccine Injury Compensation Trust Fund in its financial statements. The correction of this omission resulted in a net increase in net position of \$942 million at September 30, 1996. The Trust Fund assets are maintained by the Department of the Treasury.

During fiscal year 1997, IHS performed an extensive reconciliation of its real property. This task involved newly capitalizing certain property-in-service and construction-in-progress, and recalculations of accumulated depreciation. The resultant increase to IHS's net position was \$184 million. Other decreases of \$6 million reduced the net adjustment to \$178 million.

U.S. Department of Health and Human Services
Supplemental Consolidating Statement of Financial Position by Operating Divisions
As of September 30, 1997

(in millions)											
	HCFA	NIH	ACF	AoA	AHCPR	CDC	FDA	HRSA	IHS	SAMHSA	HHS - wide
Assets											
Entity Assets:											
Fund Balances with Treasury	\$ 13,412	\$ 11,366	\$ 22,585	\$ 229	\$ 132	\$ 2,202	\$ 361	\$ 2,962	\$ 1,108	\$ 1,674	\$ 56,345
Investments	151,085	10	-	-	-	-	-	1,196	-	-	152,291
Accounts Receivable, Net:											
From Federal Agencies	1,105	179	3	1	1	42	6	27	6	4	1,476
From the Public	2,485	3	2	-	1	2	13	375	16	19	2,916
Interest Receivable	2,849	-	-	-	-	-	-	-	-	-	2,849
Advances:											
To Federal Agencies	-	76	-	17	-	3	3	24	-	-	136
To the Public	12	28	-	6	-	17	-	-	40	-	103
Inventories	-	13	-	-	-	30	-	-	15	-	74
Property and Equipment, Net	40	345	-	-	-	133	163	3	647	1	1,340
Non-Entity Assets:											
Accounts Receivable, Net	77	-	-	-	-	-	-	-	-	-	136
Total Assets	\$ 171,065	\$ 12,020	\$ 22,590	\$ 253	\$ 134	\$ 2,429	\$ 546	\$ 4,587	\$ 1,832	\$ 1,679	\$ 217,666
Liabilities											
Funded Liabilities:											
Payables:											
Due Federal Agencies	\$ 208	\$ 50	\$ 1	\$ -	\$ 1	\$ 8	\$ 16	\$ 10	\$ 26	\$ 10	\$ 354
Due the Public	41,764	1,476	13	-	6	87	16	607	48	8	44,196
Advances:											
From Federal Agencies	-	-	275	-	-	53	7	-	64	34	458
From the Public	-	-	106	192	16	102	1	293	-	38	755
Accrued Payroll and Benefits	15	-	6	-	1	22	31	7	30	2	130
Unfunded Liabilities:											
Annual Leave	23	70	11	1	2	34	45	16	60	4	282
Workers' Compensation Benefits	7	40	3	-	-	11	17	25	45	3	167
Other Liabilities	-	-	-	-	-	22	-	-	2	-	24
Pensions	-	-	-	-	-	-	-	-	-	-	3,296
Total Liabilities	42,017	1,636	415	194	26	339	133	958	275	99	49,662
Net Position											
Unexpended Appropriations	65	10,042	21,864	60	102	1,990	286	2,353	954	1,703	39,729
Invested Capital	40	358	-	-	-	163	163	357	662	1	1,744
Cumulative Results of Operations	128,973	94	325	-	8	4	26	960	48	(117)	130,300
Future Funding Requirements	(30)	(110)	(14)	(1)	(2)	(67)	(62)	(41)	(107)	(7)	(3,769)
Total Net Position	129,048	10,384	22,175	59	108	2,090	413	3,629	1,557	1,580	168,004
Total Liabilities & Net Position	\$ 171,065	\$ 12,020	\$ 22,590	\$ 253	\$ 134	\$ 2,429	\$ 546	\$ 4,587	\$ 1,832	\$ 1,679	\$ 217,666

U.S. Department of Health and Human Services
Supplemental Consolidating Statement of Operations
and Changes in Net Position by Operating Divisions
For the Fiscal Year Ended September 30, 1997

(in millions)

Revenues and Financial Sources

	HCFA	NIH	ACF	AoA	AHCPR	CDC	FDA	HRSA
Appropriated Capital Used:								
General Appropriations	\$ 96,556	\$ 12,963	\$ 31,228	\$ 1,262	\$ 150	\$ 2,438	\$ 936	\$ 3,460
Matching Contributions	59,615	-	-	-	-	-	-	-
Employment Taxes	112,742	-	-	-	-	-	-	-
SMI Premiums Collected	19,141	-	-	-	-	-	-	-
Interest Revenue	11,900	-	-	-	-	-	-	-
Sales of Goods and Services	36	359	21	2	58	135	120	273
Imputed Financing	10	137	13	1	2	43	51	18
Other Revenue and Financing	6,051	68	-	-	-	1	-	120
Total Revenue and Financing Sources	306,051	13,527	31,262	1,265	210	2,617	1,107	3,871

Expenses

Operating:								
Personnel Costs	1,241	884	117	10	22	450	638	139
Travel and Transportation	5	24	5	-	1	31	21	6
Rent, Communications and Utilities	44	101	16	2	7	42	75	12
Printing and Reproduction	19	16	-	-	2	5	3	-
Contractual Services	1,547	2,032	457	2	89	353	180	231
Supplies and Materials	6	227	4	-	1	204	61	6
Grants	96,593	9,924	30,629	1,248	84	1,475	27	3,156
Insurance Claims and Indemnities	207,455	-	-	-	-	-	1	134
Other Operating Expenses	-	-	-	-	-	2	-	7
Depreciation and Amortization	11	30	-	-	-	10	14	-
Imputed Personnel Costs	10	137	13	1	2	43	51	18
Other Non-Operating Expenses	1,678	40	2	-	-	8	65	25
Total Expenses	308,609	13,415	31,243	1,263	208	2,623	1,136	3,734
Excess of Revenues and Financing Sources	(2,558)	112	19	2	2	(6)	(29)	137
Net Position, Beginning Balance	125,365	13,443	20,739	451	157	2,534	507	2,406
Adjustments	15,247	(3,061)	(7,288)	-	-	(312)	5	942
Net Position, Restated Beginning Balance	140,612	10,382	13,451	451	157	2,222	512	3,348
Excess of Revenues and Financing Sources	(2,558)	112	19	2	2	(6)	(29)	137
Non-Operating Changes	(9,006)	(110)	8,705	(394)	(51)	(126)	(70)	144
Net Position, Ending Balance	\$ 129,048	\$ 10,384	\$ 22,175	\$ 59	\$ 108	\$ 2,090	\$ 413	\$ 3,629

U.S. Department of Health and Human Services
Supplemental Consolidating Statement of Operations
and Changes in Net Position by Operating Divisions
For the Fiscal Year Ended September 30, 1997

<i>(in millions)</i>	IHS	SAMHSA	OS	PSC	Intra- HHS	HHS - wide
Revenues and Financial Sources						
Appropriated Capital Used:						
General Appropriations	\$ 2,135	\$ 1,996	\$ 195	\$ 180	\$ -	\$ 153,499
Matching Contributions	-	-	-	-	-	59,615
Employment Taxes	-	-	-	-	-	112,742
SMI Premiums Collected	-	-	-	-	-	19,141
Interest Revenue	-	-	-	-	-	11,900
Sales of Goods and Services	415	15	91	209	(334)	1,400
Imputed Financing	71	5	1	-	(40)	312
Other Revenue and Financing	-	-	-	-	-	6,240
Total Revenue and Financing Sources	2,621	2,016	287	389	(374)	364,849
Expenses						
Operating:						
Personnel Costs	755	45	135	359	(313)	4,482
Travel and Transportation	48	1	7	2	-	151
Rent, Communications and Utilities	40	6	18	47	-	410
Printing and Reproduction	1	-	-	1	-	47
Contractual Services	851	150	80	94	(10)	6,056
Supplies and Materials	180	1	4	6	(11)	689
Grants	605	1,805	45	-	-	145,591
Insurance Claims and Indemnities	1	1	-	-	-	207,592
Other Operating Expenses	-	-	-	32	-	41
Depreciation and Amortization	24	-	-	1	-	90
Imputed Personnel Costs	71	5	1	-	(40)	312
Other Non-Operating Expenses	1	-	-	2	-	1,821
Total Expenses	2,577	2,014	290	544	(374)	367,282
Excess of Revenues and Financing Sources	44	2	(3)	(155)		(2,433)
Net Position, Beginning Balance	1,481	1,264	251	(3,053)		165,545
Adjustments	178	-	-	-		5,711
Net Position, Restated Beginning Balance	1,659	1,264	251	(3,053)		171,256
Excess of Revenues and Financing Sources	44	2	(3)	(155)		(2,433)
Non-Operating Changes	(146)	314	6	(85)		(819)
Net Position, Ending Balance	\$ 1,557	\$ 1,580	\$ 254	\$ (3,293)		\$ 168,004